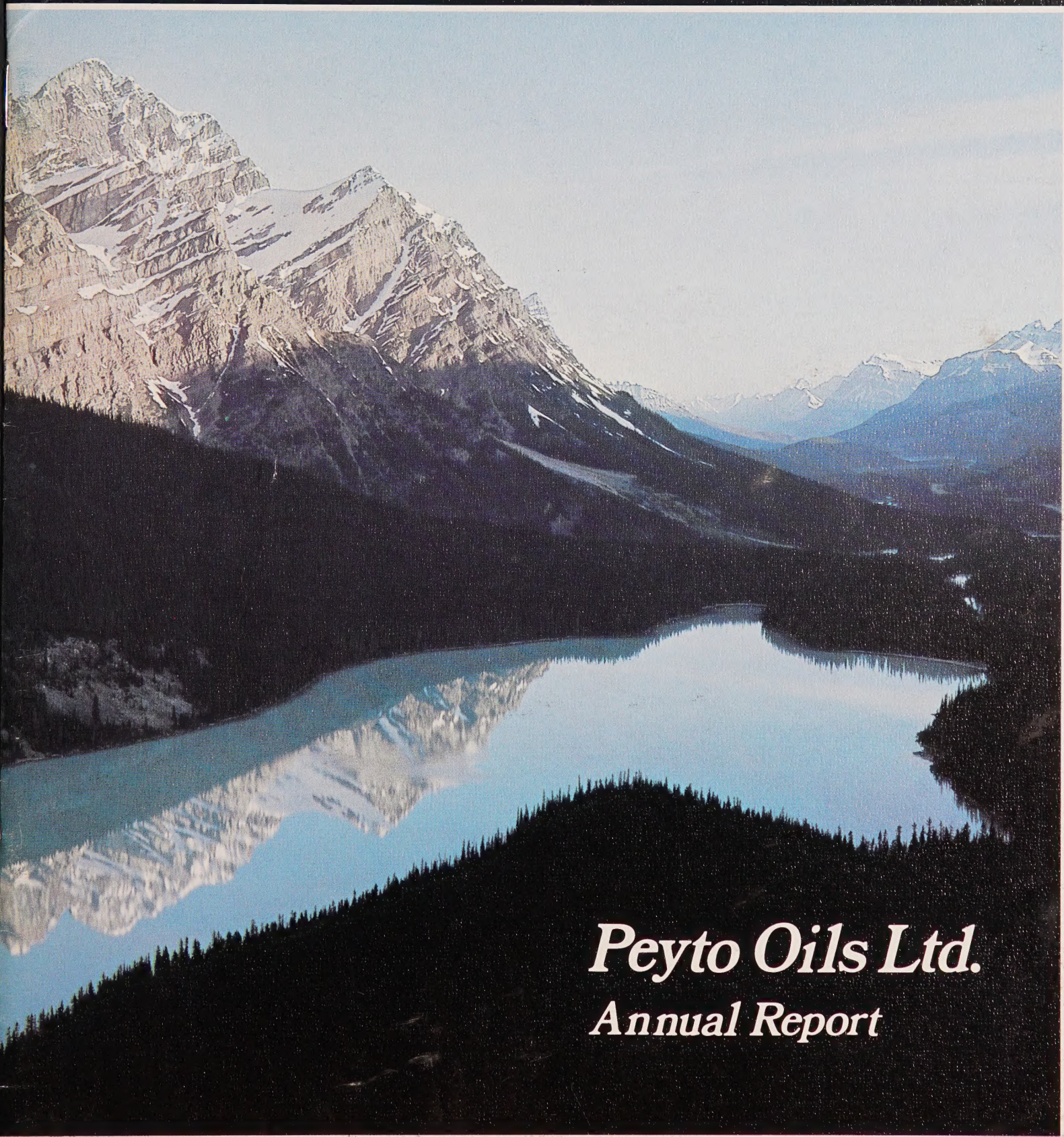


YEAR ENDING MAY 31st, 1977



Peyto Oils Ltd.
Annual Report

Peyto Oils Ltd. and Subsidiaries

Peyto Explorations Inc.	100%
Polaris Oil Limited	100%
Peyto Oils (U.K.) Ltd.	100%
Giant Reef Petroleums Limited	82%
Not included in consolidation:	
Enjay Holdings Limited	(40%)
Incorporated	
Alberta May 19, 1966	

HEAD OFFICE:

Suite 1650, 633 - 6th Avenue S.W.
CALGARY, Alberta T2P 2Y5
Area Code 403 261-5042

OFFICERS:

R. T. VANDERHAM — President
K. D. MOORE — Vice-President
W. C. KERR — Secretary
J. E. MORRISH — Assistant Secretary

DIRECTORS:

CARMEN W. BYLER
JEAN Le REUN
R. T. VANDERHAM
W. WOLODARSKY

BANKERS:

BANK OF MONTREAL
604 - 8th Ave. S.W.
CALGARY, Alberta T2P 1G4

REGISTRAR AND TRANSFER AGENT:

MONTREAL TRUST COMPANY
411 - 8th Ave. S.W.
CALGARY, Alberta T2P 1E7
15 King St. West
TORONTO, Ontario M5H 1B4

AUDITORS:

PEAT, MARWICK, MITCHELL & CO.
2500, 700 - 2nd Street S.W.
CALGARY, Alberta T2P 2W2

STOCK LISTING:

TORONTO STOCK EXCHANGE

OUR COVER:

"PEYTO LAKE" — located 27 miles north of Lake Louise on the Banff-Jasper Highway in Banff National Park. The pale blue color of the lake is a result of the silt carried in the outwash of Peyto Glacier. ALBERTA, Canada.

GLOSSARY

- Barrel of oil —**
the standard measure of crude oil volume being 35 Imperial gallons or 42 U.S. gallons.
- BOPD —**
barrels oil per day.
- Commercial discovery —**
a test well from which petroleum substances may be produced in sufficient quantities to justify completing the test well for the taking of production.
- Development drilling —**
additional wells drilled following a discovery for the purpose of delineating the areal extent of the new field or pool.
- Dry and abandoned —**
a drilled well which has no economic value.
- Exploratory drilling (or wildcat) —**
drilling for oil or gas in an area or at a subsurface depth previously unexplored.
- Farmout —**
an agreement whereby a company (farmee) earns an interest in mineral rights held by another company (farmor) by the carrying out of certain exploration work usually involving a test well.
- Geological and geophysical structure —**
a fold, fault or other deformation of the earth's crust.
- Lease (acreage, Production Licence, Prospecting Licence, Concession) —**
rights granted covering specific geographic areas by owner for the exploration and production of petroleum and natural gas, or other minerals.
- Liquids — L.P.G.'s —**
Liquified Petroleum gases, as distinguished from crude oil, contained in some natural gas usually requiring a processing plant to separate from natural gas.
- Mcf —**
a volumetric measure containing one thousand cubic feet of natural gas.
- MMcf**
a volumetric measure containing one million cubic feet of natural gas.
- Sour gas —**
natural gas containing hydrogen sulphide (H₂S) highly toxic and requiring processing before sale.
- Seismic — seismograph survey —**
a technique used to determine the configuration of subsurface geological structures.
- Ton of sulphur —**
actually a long ton or 2,204 lbs.
- Wellhead price —**
the price paid to the producer by the buyer of crude oil or natural gas exclusive of all transportation charges.
- Working interest —**
that percentage interest which the company benefits from or is liable for.

Five Year Financial & Operating Review

	1977	1976	1975	1974	1973
Total Revenue	\$ 3,880,000	\$ 2,472,000	\$1,271,000	\$ 672,000	\$ 581,000
Cash Flow	2,341,000	1,405,000	800,000	204,000	90,000
Cash Flow/Share	83¢	50¢	28¢	7¢	4¢
Depreciation/Depletion	762,000	479,000	246,000	226,000	159,000
Net Income (loss)	736,000	474,000	183,000	(292,000)	(249,000)
Net Income (loss)/share	26¢	17¢	6¢	(10¢)	(11¢)
Total Assets	13,500,000	13,000,000	7,002,000	6,437,000	4,751,000
Working Capital	1,370,000	1,089,000	2,364,000	2,449,432	634,362
Long-term Debt	5,000,000	5,830,000	370,000	604,000	832,000
Shares Outstanding	2,843,583	2,833,583	2,831,383	2,831,383	2,431,383
Shareholder's Equity	6,979,000	6,205,000	5,726,000	5,543,000	3,622,000
Toronto Stock Exchange					
Share Volume*	1,766,710		1,206,795	2,559,131	2,682,900
Value*	\$ 8,551,880		\$4,421,874	\$17,398,833	
Gross wells drilled	21	20	13	20	23
Oil/Gas	13	11	9	10	11
Dry and Abandoned	8	9	4	10	12
Number of Employees	6	5	4	5	5
Proven Oil & Condensate ...	3,639,980	3,945,682			
Probable Oil & Condensate .	2,065,238	2,574,853			
Total in Barrels	5,705,218	6,520,537			
Proven Gas	49,531**	42,330**			
Probable Gas	13,961	11,201			
Total in MMcf	63,492	53,531			
Proven Sulphur	110,393	93,305			
Probable Sulphur	56,651	56,905			
Total in Tons	167,044	150,210			

* Calendar Year

** not inclusive of 32,000 MMcf attributable to the revenues allocated to Turner Valley Gas Plant from which 15¢/Mcf is collected when processed.



Dear Shareholder:

Continuing sharp increases in prices received for the company's oil and natural gas production coupled with increasing volumes from new production coming on stream produced most gratifying results for the fiscal year ending May 31, 1977 for your company and its subsidiaries.

Revenues from oil and gas sales after royalties reached \$3,880,000, cash flow was \$2,341,000 and net earnings increased to \$736,000 or 26 cents per share. Production averaged 856 barrels of oil and 6 MMcf of gas per day.

Revenues were adversely affected due to the existence of a temporary gas surplus in Alberta resulting in lower sales from some of the company's properties. It is expected that these surplus conditions will disappear over a 2 to 3 year period.

To supplement the funds available for exploration from its internally generated cash flow your company entered into a "Drilling Fund" agreement with certain investors from West Germany. Up to a maximum of \$3 million will be made available to your company during 1977 and 1978. These drilling funds will greatly enlarge your company's exploration potential and has already proven to be highly beneficial. As consideration for obtaining these funds your company granted a stock option to the fund managers (see note 4 to the final statement).

Continued stability in the industry from a political standpoint, together with greater profitability from oil and gas production has resulted in boom conditions in this province's oil industry. Prices for oil and gas leases and exploration licenses have soared to unprecedented heights. The costs of drilling, due partly to the high demand for drilling rigs, have also risen sharply. The industry presently is highly competitive with expenditures in exploration running at an all time high.

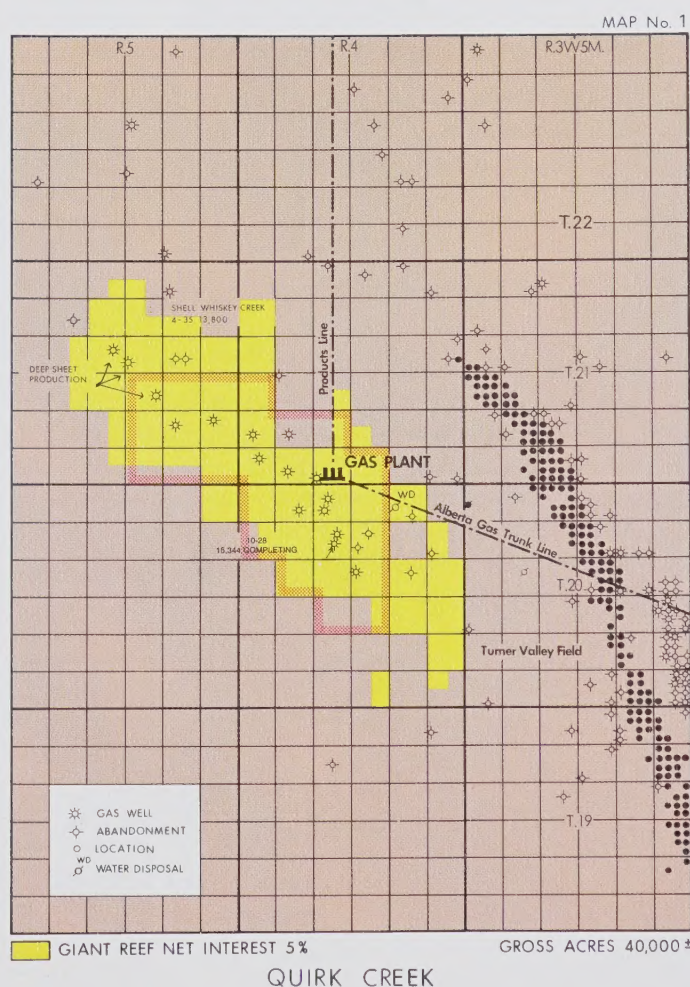
Your company has continued to actively pursue both development prospects which offer relatively near term income and exploration prospects from which income may be derived in the future. Exploration activities have remained primarily in Western Canada with most emphasis on Alberta. However, due to extremely high prices for exploration land in Western Canada your company is shifting some of its exploration efforts to the United States.

EXPLORATION AND DEVELOPMENT Western Canada

Quirk Creek (See Map No. 1)

The Husky et al Quirk Creek 10-28-20-4W5 well, after 8 months of drilling, reached its projected total depth of 15,344 feet. The well encountered pay zones in the Mississippian as well as some indications of hydrocarbons in the Wabamun and Leduc formations. The well is currently being evaluated in the deeper zones and will probably be completed as a gas producer in the Mississippian zone. The well is the most expensive onshore well in which your company has participated. Drilling costs were \$3.5 million and completion operations will cost an additional \$600,000. Giant Reef, your company's 82% owned subsidiary, owns a 5% interest in this well and in the Quirk Creek field.

One or possibly two deep wells and some shallow infill drilling will be carried out in the coming year.



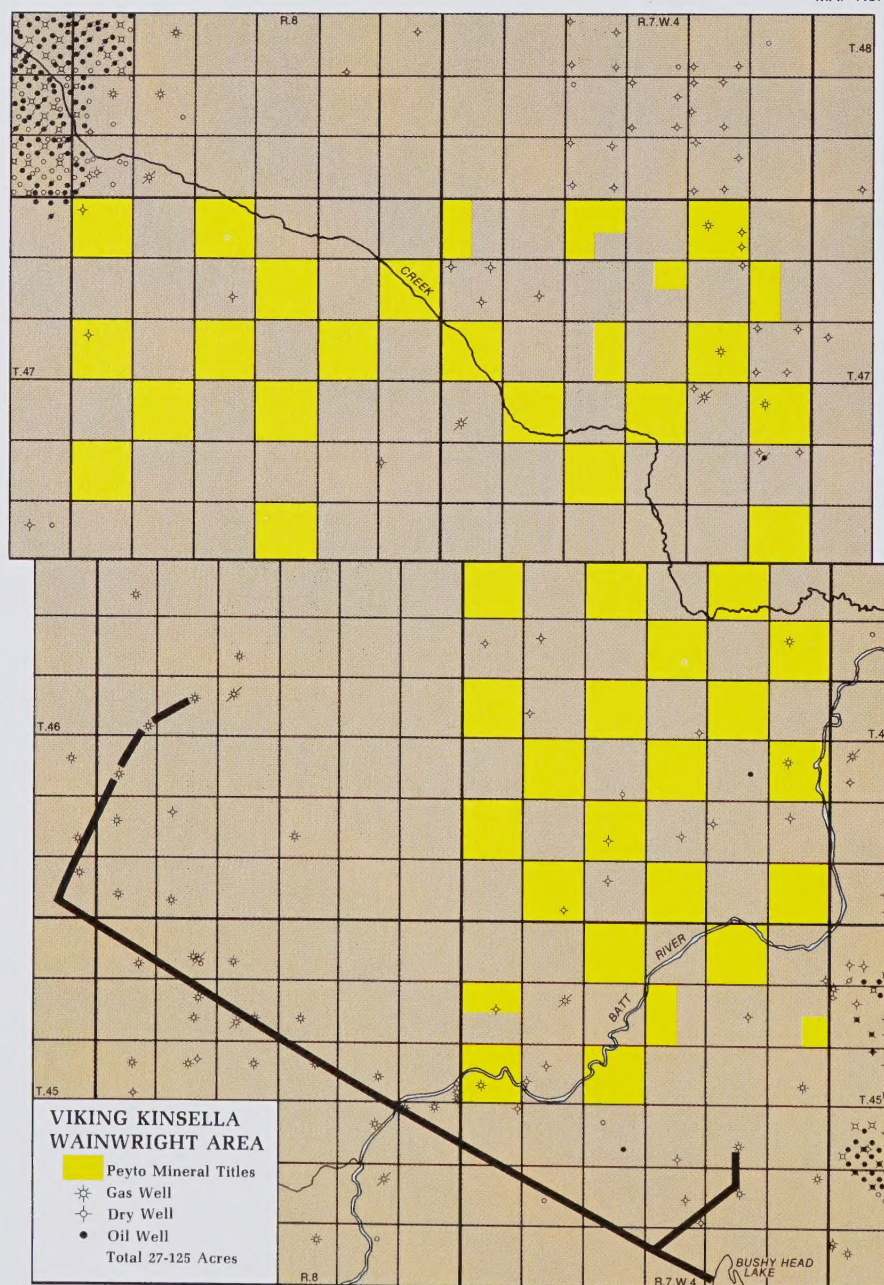
Long Coulee

The new 30 MMcf/d gas processing plant commenced operations in April 1977. Your company's share of the production is approximately 1 MMcf/d. Subsequently our gas reserves in this area were substantially increased by the purchase of a 640 acre lease which when drilled proved to contain approximately 10 billion cubic feet of gas and substantial gas liquids. We are presently awaiting a gas purchase contract. Peyto's interest in this production will be 38.75%. Additional plant capacity will be required to process these new reserves.

Lacombe

The new 6 MMcf/d gas plant went on production in January 1977 and operated until April. At that time the gas purchaser advised that no market for the gas would be available until November. However, in June the company and its partners negotiated a short term reduced price contract to run until November when the original contract again comes into effect. In this manner the company was able to maintain production and reduce the shut-in time to a minimum.

MAP No. 2



Viking Kinsella (See Map No. 2)

Eight wells were drilled on the company's 27,125 acres of mineral titles resulting in 5 gaswells and 3 abandonments. This area is currently being explored by the industry and it is anticipated that the additional reserves being established will soon justify construction of pipeline gathering facilities.

Seebe-Ghost

The gas plant site selection and design studies have been completed. Timing of actual plant construction will be determined by availability of gas contracts and anticipated market demands.

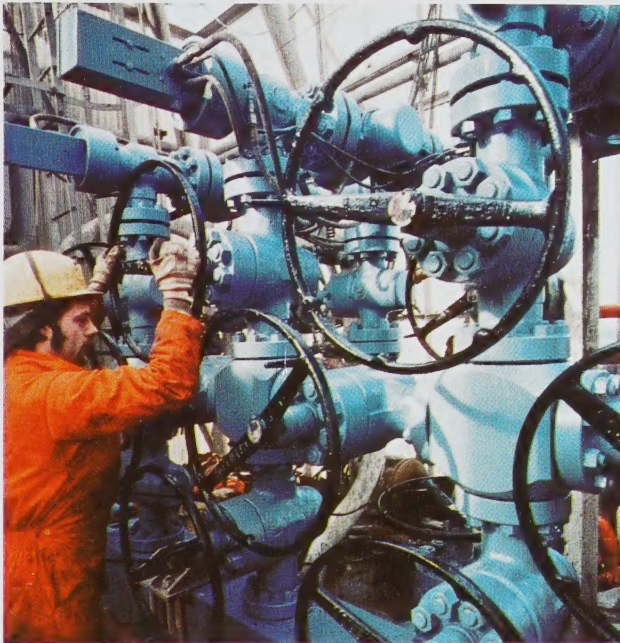


Photo courtesy of British Petroleum.

FOREIGN EXPLORATION

United Kingdom (see centerfold map) Block 3/7

Following the drilling and completion of wells 3/7-1 and 3/7-2, each flowing approximately 3000 BOPD, the operator Chevron-Standard is now drilling well 3/7-3 on the south boundary of the block. Shell-Esso, lessee's of Block 3/12, are contributing substantially towards the cost of the latest well in which Peyto Oils (U.K.) Limited, our wholly owned subsidiary, holds a 3.5% working interest.

Although both 3/7-1 and 3/7-2 flowed substantial quantities of oil their commercial value remains in doubt at present. It is hoped that at a later date this oil can be piped via subsea completions to the adjoining Ninian production platform.

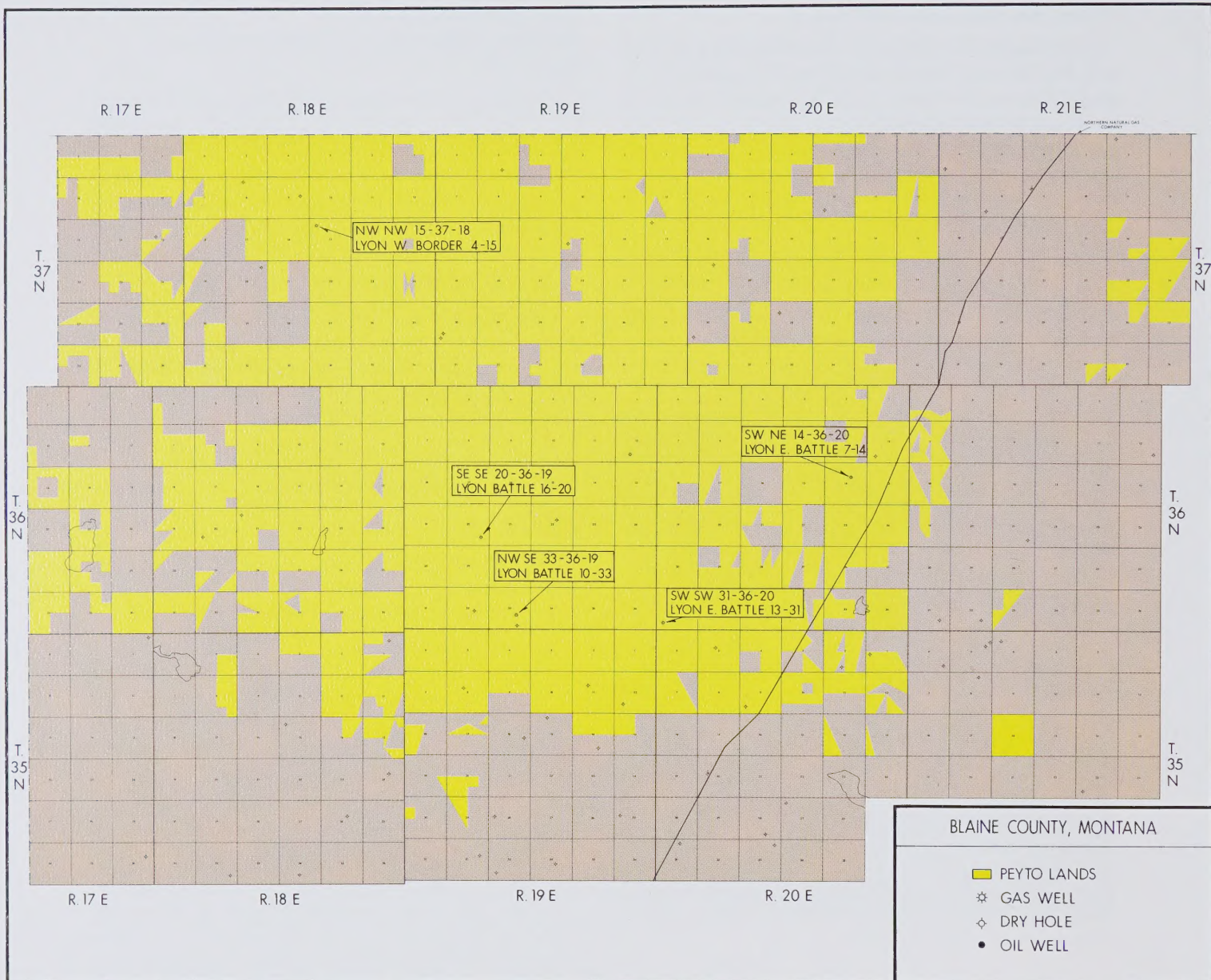
Results of the currently drilling 3/7-3 well should be known by October 1977.

Block 211/2

The arrival of the rig "Sea Conquest" is expected the second week in September. This rig is presently drilling at another North Sea location.

British Petroleum, our farmee on Block 211/2, will drill the first well on this block at their sole risk and expense, as soon as the "Sea Conquest" becomes available. The well will be drilled in 1,100 feet of water to a depth of +13,500 feet to test the Jurassic Sands, known to be productive in some of the giant oilfields in the North Sea such as Brent, Stratford, Magnus and Ninian.

B.P.'s "Sea Conquest" is one of the newest semi-submersible rigs currently in service (see accompanying photo). It was especially built to withstand the severe storms in the North Sea and is equipped with Blow-Out Preventers capable of controlling well pressures up to 15,000 pound per square inch. A photo of the Blow-Out Preventers of which only two are in existence are shown in this report.



UNITED STATES

Montana (See Map No. 3)

Your company's wholly owned U.S. subsidiary Peyto Explorations Inc. together with its drilling fund partner, participated in a two-well program in Blaine County, Montana. Gas was discovered in three zones at a depth from 1,500 to 1,700 feet. Subsequent drilling has given every indication that a commercial gas field has been discovered. Maximum test rates of 2.5 and 3.1 MMcf/d were encountered in 2 of the 6 wells drilled to date. All wells were cased and 4 need stimulation and

further evaluation. Due to the proximity of a major gas transmission line early production is anticipated. The company and its partners control 120,000 acres of leases in this area. Peyto's net interest in this production is 18%.

A drilling program will begin shortly. Gas contract negotiations have been commenced and after last winter's energy crisis in the U.S. these negotiations should be readily concluded.

California — Onshore

Your company (25%) will participate in a well to be commenced shortly at Cuyama in Santa Barbara County, California.

Indiana

Peyto Explorations Inc. (12½%) is a participant in a 7 well shallow drilling program in northeast Indiana. The drilling is designed to evaluate deeper zones below a previously producing oilfield. Approximately 5,000 acres are involved in the play.

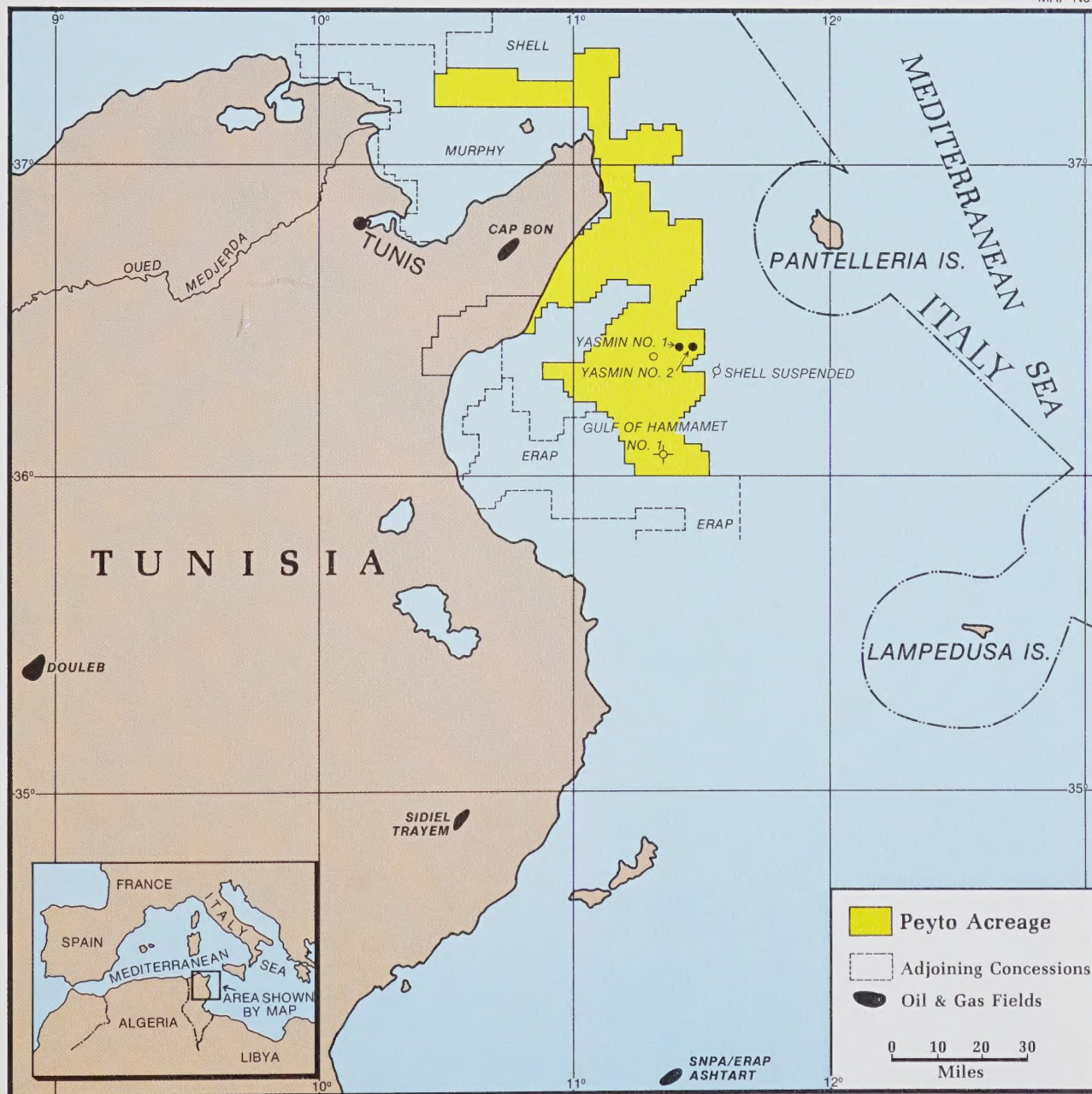
Tunisia (See Map No. 4)

A third well, Yasmin #2, the first followup to a small oil discovery made last year and renamed

Yasmin #1, has been completed on a 1.2 million acre concession in which your company's, together with one of its subsidiaries, interest is 1.7858%. Yasmin #2 is currently being evaluated.

The Yasmin #1 (formerly Gulf of Hammamet #2) flowed 1,790 barrels of oil and was suspended. Additional drilling will be required to determine development and production possibility. This small pool is located in 400 feet of water and some 35 miles offshore. Your company is in a carried working interest position through the current two well program.

MAP No. 4



NORTH SEA AREA

Peyto et al Lands

Oil Fields

Gas Fields

Location of Drilling Wells

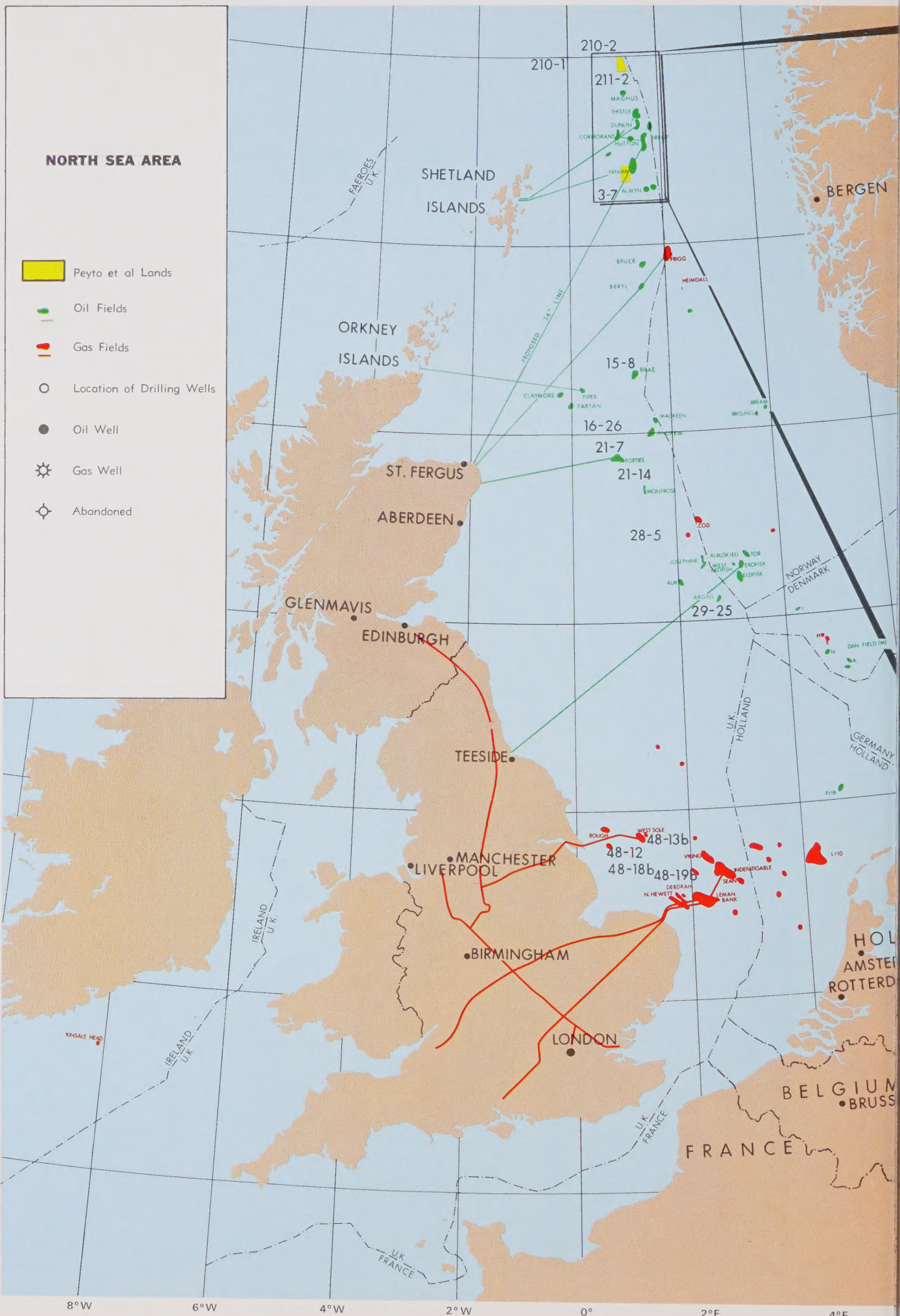
Oil Well

+

Gas Well

x

Abandoned





Cameroon, West Africa (See Map No. 5)

A 50% interest in this concession containing 185,200 acres has been farmed out to a major oil company in exchange for an extensive seismic survey to be conducted by the farmee for not less than \$1 million. After completion of the survey Peyto's interest will be 3.375%.

Australia

Two offshore concessions of 5,127,325 acres and 4,446,720 acres respectively were obtained off the West Coast of Australia. A preliminary seismic study is underway. Peyto's interest in this acreage is 10%.

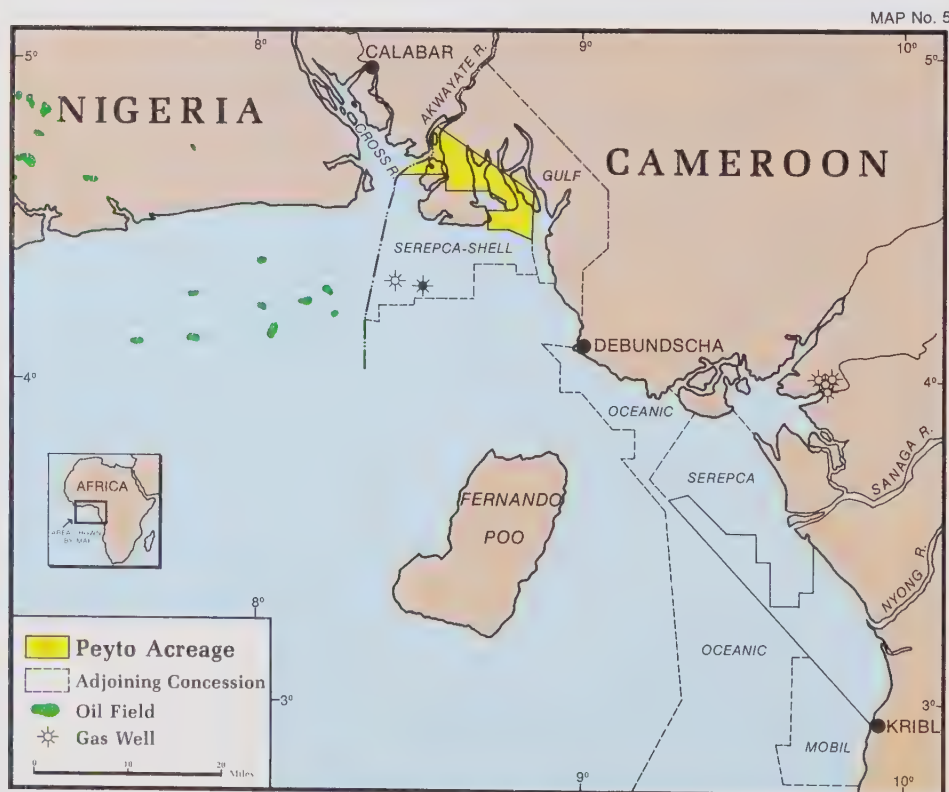
It is with great regret and sadness that we inform you of the recent death of our dear friend and director Mr. Al McCruden. Mr. McCruden was one of the founding shareholders, the company Secretary and a Director. His friendship and advice which all the members of the staff and the Board of Directors enjoyed and appreciated will be sorely missed.

Mr. William C. Kerr has been appointed Secretary of the Company and Mr. David Keefe has joined the company as landman.

Your Board wishes to thank the company's employees for their dedication and co-operation during the past year.

Submitted on behalf of the Board of Directors

Robert T. M. Vanderham,
President.



Peyto Oils Ltd. and Subsidiaries

Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of Peyto Oils Ltd. as at May 31, 1977 and the consolidated statements of earnings, retained earnings (deficit) and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at May 31, 1977 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Calgary, Canada
August 3, 1977

Peat, Marwick, Mitchell & Co.
Chartered Accountants

Peyto Oils Ltd. and Subsidiaries

Consolidated Balance Sheet May 31, 1977 (with comparative figures for 1976)

ASSETS

	1977	1976
Current assets:		
Cash	\$ 26,357	31,961
Deposit receipts, including accrued interest	806,217	1,007,771
Accounts receivable	964,395	644,483
Total current assets	<u>1,796,969</u>	<u>1,684,215</u>
Property, plant and equipment, at cost		
(Notes 2 and 3)	13,584,634	12,378,039
Less accumulated depletion and depreciation	2,122,402	1,360,460
	<u>11,462,232</u>	<u>11,017,579</u>
Other assets:		
Investments, at cost less amounts written-off		
(quoted market value \$126,747; 1976 \$343,696)	111,148	240,256
Other investments, at cost less amounts		
written off (no quoted market value)	115,726	77,216
Refundable deposits	11,034	14,198
Incorporation costs	10,039	10,039
	<u>247,947</u>	<u>341,709</u>
	<u>\$13,507,148</u>	<u>13,043,503</u>

LIABILITIES

	1977	1976
Current liabilities:		
Accounts payable and accrued liabilities	\$ 254,416	420,240
Current portion of bank loans (Note 3)	114,108	175,000
Income taxes payable, subsidiary company	58,000	—
Total current liabilities	426,524	595,240
Bank loans, net of current portion (Note 3)	5,000,000	5,830,000
Minority interest in subsidiary company	237,896	167,449
Deferred revenue	119,400	—
Deferred income taxes	743,391	245,391
Shareholders' equity:		
Share capital (Note 4):		
Shares without nominal or par value.		
Authorized 6,000,000 shares: issued		
2,843,583 shares (1976 — 2,833,583 shares)	6,265,977	6,227,477
Retained earnings (deficit)	713,960	(22,054)
	6,979,937	6,205,423
	<u>\$13,507,148</u>	<u>13,043,503</u>

Approved on behalf of the Board:

R. T. VANDERHAM , Director

W. WOLODARSKY , Director

See accompanying notes.

Peyto Oils Ltd. and Subsidiaries

Consolidated Statement of Earnings Year ended May 31, 1977 (with comparative figures for 1976)

	1977	1976
Revenue:		
Oil and gas	\$ 3,880,448	2,270,915
Interest earned	88,817	131,247
Management and other income	64,730	33,224
Gain on sale of properties and investments	56,067	36,264
	<u>4,090,062</u>	<u>2,471,650</u>
Expenses:		
Operating	927,847	590,519
Lease rentals on non-producing properties	45,246	38,152
General and administrative	252,210	219,840
Interest — bank loan	625,166	312,109
Depletion	531,027	347,695
Depreciation	230,914	131,692
Dryholes and abandonments	209,409	221,047
	<u>2,821,819</u>	<u>1,861,054</u>
Earnings before income taxes, minority interest and extraordinary item	<u>1,268,243</u>	<u>610,596</u>
Income taxes (Note 5):		
Current	58,000	—
Deferred	498,000	266,354
Province of Alberta Royalty Credit	(216,118)	(130,490)
	<u>339,882</u>	<u>135,864</u>
Earnings before minority interest and extraordinary item	<u>928,361</u>	<u>474,732</u>
Minority interest in earnings of subsidiary	<u>70,447</u>	<u>38,907</u>
Earnings before extraordinary item	<u>857,914</u>	<u>435,825</u>
Extraordinary item:		
Reduction of deferred income taxes resulting from the application of exploration and development expenses	—	38,051
Write down of certain investments to market value	121,900	—
Net earnings	<u>\$ 736,014</u>	<u>473,876</u>
Net earnings per share (Note 6):		
Before extraordinary item	\$ 0.30	0.16
Extraordinary item	(0.04)	0.01
	<u>\$ 0.26</u>	<u>0.17</u>

See accompanying notes.

Peyto Oils Ltd. and Subsidiaries

Consolidated Statement of Changes in Financial Position Year ended May 31, 1977 (with comparative figures for 1976)

	1977	1976
Working capital was provided from:		
Net earnings before extraordinary item	\$ 857,914	435,825
Add items not affecting working capital	1,483,730	969,431
Working capital provided from operations	2,341,644	1,405,256
Increase in deferred revenue	119,400	—
Issue of share capital	38,500	5,467
Proceeds from bank loan	—	5,580,000
Proceeds on sale of properties and investments	82,652	249,253
	<u>2,582,196</u>	<u>7,239,976</u>
Working capital was used for:		
Property, plant and equipment	1,435,390	8,095,710
Decrease in bank loans	830,000	120,000
Increase in other assets	35,336	54,410
Purchase of additional shares of a subsidiary	—	244,508
	<u>2,300,726</u>	<u>8,514,628</u>
Increase (decrease) in working capital	281,470	(1,274,652)
Working capital, beginning of year	1,088,975	2,363,627
Working capital, end of year	<u>\$1,370,445</u>	<u>1,088,975</u>

Consolidated Statement of Retained Earnings (Deficit) Year ended May 31, 1977 (with comparative figures for 1976)

	1977	1976
Deficit, beginning of year	\$ 22,054	495,930
Net earnings	736,014	473,876
Retained earnings (deficit), end of year	<u>\$ 713,960</u>	<u>(22,054)</u>

See accompanying notes.

Notes to the Consolidated Financial Statements May 31, 1977

1. Significant accounting policies:

Principles of Consolidation:

The consolidated financial statements include the accounts of all wholly-owned subsidiary companies and an 82% held subsidiary, Giant Reef Petroleums Limited.

The excess of the purchase price of the shares of Giant Reef Petroleums Limited over the underlying net book values, at dates of acquisition, has, on consolidation, been added to the cost of developed oil and gas properties and is being depleted on the unit-of-production method.

Petroleum and Natural Gas Properties:

Under the successful efforts method of accounting as used by the company (as opposed to the "full cost" method) all costs relative to exploration and development of petroleum and natural gas whether productive or non-productive are initially capitalized. The cost of non-producing properties, including development and exploration thereon, less any proceeds on disposal, are charged against earnings in the year of disposal, abandonment or surrender. Costs pertaining to producing properties are depleted on a unit-of-production method based on estimated proven reserves. Carrying costs on undeveloped properties are charged against earnings in the year incurred.

Depreciation:

Lease and well equipment and gas plants are being depreciated on the composite unit-of-production method. A subsidiary company's gas plant is being depreciated on the straight-line basis using a rate of 5 percent per annum.

Income taxes:

The company follows the tax allocation basis of accounting for all timing differences between net earnings and taxable income.

2. Property, plant and equipment:

	1977		1976	
	Assets at cost	Accumulated depreciation and depletion	Net	Net
Developed oil and gas properties and equipment thereon	\$10,084,922	1,635,365	8,449,557	8,409,480
Gas plants	2,528,094	487,037	2,041,057	1,885,487
Undeveloped oil, gas and mineral properties	971,618	—	971,618	722,612
	<u>\$13,584,634</u>	<u>2,122,402</u>	<u>11,462,232</u>	<u>11,017,579</u>

3. The bank loans are evidenced by demand promissory notes and are secured by certain petroleum and natural gas properties and accounts receivable. A production bank loan in the amount of \$5,000,000 is repayable out of future production proceeds, and, accordingly, is not expected to require the use of existing working capital; therefore, no portion of this loan has been reclassified to current liabilities. Principal payments required to meet the next fiscal year's instalment on this loan are estimated at \$575,000.

4. Share capital:

During the year the company issued 10,000 shares to an employee under a stock purchase agreement at a price of \$3.85 per share payable in instalments over ten years.

At May 31, 1977 the company has reserved 13,300 shares for employee stock options. The options are exercisable one fifth each year on a cumulative basis at a price of \$2.485 per share, expiring on September 5, 1979 or 60 days after termination of employment whichever comes first.

Under a drilling program agreement, the company has granted options to purchase up to 160,000 shares at a price of \$5.50 per share. The options expire on December 30, 1978.

5. Income taxes:

At May 31, 1977 the following amounts remain to be carried forward and applied against future taxable income to the maximum amounts permitted annually under the Income Tax Act.

Drilling, exploration and lease acquisition costs to May 6, 1974	\$1,186,140
Cumulative Canadian Exploration Expenditures	\$ 88,449
Cumulative Canadian Development Expenditures	\$5,726,159
Foreign exploration and development expenditures	\$ 367,683
Undepreciated capital cost	\$1,093,757

6. Net earnings per share:

The net earnings per share is calculated using the weighted average number of shares outstanding during the year. Fully diluted earnings per share are not presented as there would be no material change.

7. Anti-Inflation:

The company is subject to the provisions of the Anti-Inflation Act and Regulations governing the amount of dividend payments and as a result the amount of dividends which may be paid is restricted.

8. Remuneration of directors and officers:

The aggregate remuneration paid to senior officers (as defined by The Companies Act, Alberta, which term includes the five highest paid employees of the company) during the year amounted to \$110,327 (1976 — \$90,500). No remuneration was paid to directors as such.

